

**BEFORE THE COMMISSIONER OF FINANCIAL INSTITUTIONS
STATE OF TENNESSEE**

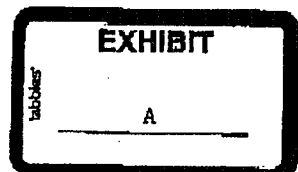
IN THE MATTER OF:)
)
SENTINEL TRUST COMPANY,)
Hohenwald, Tennessee,)
)
AND)
)
Danny N. Bates, Clifton T. Bates,)
Howard W. Cochran, Bradley S. Lancaster,)
Gary L. O'Brien,)
)
Members of the Board of Directors of)
Sentinel Trust Company,)
Hohenwald, Tennessee,)
)
Respondent.)

SWORN AFFIDAVIT OF VIVIAN S. LAMB

**STATE OF TENNESSEE
COUNTY OF DAVIDSON**

I, Vivian S. Lamb, after being duly sworn according to law and do hereby make oath and depose as follows:

1. I am the Program Administrator for the Trust Examination Division of the Tennessee Department of Financial Institutions (the "Department").
2. As Program Administrator, I am responsible for supervising and conducting examinations of Tennessee trust companies pursuant to the provisions of Tennessee Code Annotated, Sections 45-2-1602 and 45-1-124(b).
3. On June 16, 2003, the Department began an examination of Sentinel Trust Company. During the examination, Sentinel's audit firm, Charles Welch and Associates, Nashville, withdrew and declined to complete the December 31, 2002 audit of the company due to the inability to obtain evidence needed to evaluate the fair value of certain receivables. The Department's trust examiner has been unable to determine the accuracy and validity of fiduciary cash reconcilements and other corporate and fiduciary financial statements and records in order to determine the solvency of the company.



4. The Commissioner met with the Board of Sentinel Trust on October 6, 2003 to discuss the urgency of obtaining a financial statement audit.
5. Thereafter, on October 10, 2003, Sentinel President Danny Bates advised the Department's trust examiner that Kraft CPAs, ("Kraft") located in Columbia, Tennessee had been engaged to perform an audit of the company as required by T.C.A. § 45-2-402(c) and Department Bulletin B-02-2 as of December 31, 2002.
6. Subsequently, Kraft advised the Department's trust examiner that the audit was impeded due to the inadequacy and questionable accuracy of Sentinel's fiduciary and corporate cash records and reconcilements.
7. Kraft informed the Department that Sentinel had retained an independent contractor to reconcile the corporate and fiduciary accounts.
8. On January 7, 2004, Kraft issued an audit report as of December 31, 2002. The Department obtained a copy of the audit on March 19, 2004.
9. As of the December 31, 2002 audit, Kraft identified fiduciary accounts receivable of approximately \$9.4 million, of which approximately \$7.5 million resulted from expenditures made in connection with defaulted bond issues and related unreimbursed costs and expenses. The Auditors stated that the company's records were not adequate for them to satisfy themselves as to the existence, amount or collectability of these receivables. Kraft noted that Sentinel has a fiduciary duty, as trustee, to safeguard assets under administration and could be held responsible for any shortfalls. Kraft could not determine the liability, if any, which could result from the ultimate resolution of this matter.
10. Because of the materiality of the matter discussed in item 9 above, Kraft declined to give an opinion because Kraft stated that the scope of their work was not sufficient to enable them to express, and they did not express, an opinion on the financial statement of Sentinel Trust Company. Kraft has commenced an audit as of December 31, 2003, but to our knowledge, this audit has not been completed.
11. As the Department understands and as Kraft's audit noted, in the normal course of business Sentinel makes various commitments and incurs certain contingent liabilities that are not represented on its balance sheet. As of the December 31, 2002 audit, Kraft noted that Sentinel was a defendant in a lawsuit alleging breach of its fiduciary duties in connection with the issuance of certain corporate notes. Kraft further noted that counsel for Sentinel has asserted that an award of damages is unlikely, but could reach \$2,500,000.
12. On April 5, 2004, the Department sent a letter to Sentinel requesting an opinion of counsel regarding Sentinel's practice of funding defaulted bond expenses with funds from other non-related bond issues (See Attachment 1). This letter stated that it was the Department's understanding that Sentinel serves as the indenture

trustee for various high-yield, unregistered municipal and corporate bonds. In some instances, the debtor fails to make the scheduled principal and interest payments and default is declared per the terms of the indenture. Oftentimes the debtor will seek bankruptcy protection, which triggers an automatic stay and prevents any action from creditors until a plan of reorganization, debt restructuring and/or sale of collateral is approved by the bankruptcy court.

Further, the Department stated that it was its understanding that Sentinel, in its role as indenture trustee, in many instances funds various expenses relative to these defaulted issues, such as insurance, security, legal and other professional fees, in an effort to protect the value of the underlying collateral. The governing indenture and/or bondholder indemnification usually provides for the reimbursement of these expenses from the proceeds of the sale of the collateral. However, since Sentinel does not have adequate corporate liquidity to fund these expenses, it appears that Sentinel usually "borrows" from other non-related bond issues to fund these expenses. This is done by writing checks and/or wires on a pooled demand deposit account held at SunTrust Bank, Orlando, Florida. President Bates has stated that this is a "common industry" practice. Finally, the letter requested that Sentinel provide a written legal opinion addressing the legal basis of such practice.

13. In response to the April 5, 2004 letter, Sentinel's counsel requested a meeting with the Commissioner. On April 28, 2004 Sentinel's Executive Vice President Paul Williams and Sentinel's attorneys Alex Buchanan and David Lemke met with the Commissioner. At this meeting, Counsel for Sentinel indicated that the practice of funding defaulted bond expenses with funds from other non-related bond issues was inappropriate. They indicated that the expenses attributable to defaulted bonds are typically funded with corporate assets.
14. At the April 28, 2004 meeting, counsel, on behalf of Sentinel, requested permission for Sentinel to continue on a temporary basis the practice of "borrowing" funds from one bond issue to cover the expenses of unrelated defaulted bond issues. The Commissioner declined to approve that request.
15. Counsel for Sentinel also stated at the April 28, 2004 meeting that Sentinel's fiduciary cash shortfall is believed to be between \$8-10 million.
16. On April 30, 2004 the five members of Sentinel's Board and their counsel met with the Commissioner. At that meeting President Danny Bates stated that Sentinel's most recent calculations show that Sentinel had a deficit fiduciary cash position of seven million two hundred fifty thousand dollars (\$7,250,000). However, Mr. Bates indicated that this figure fluctuates daily. Finally, Mr. Bates stated that Sentinel's corporate cash account had a current balance of fifty three thousand dollars (\$53,000). The Department believes that this amount of cash is inadequate to pay the operating capital needed for the administration of the defaulted bonds for the immediate future.

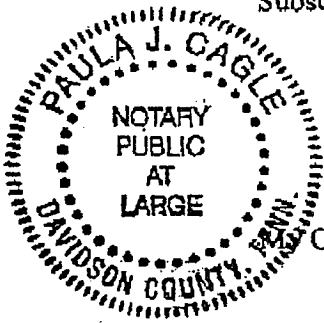
Further, the affiant sayeth not.

Dated this 3rd day of May, 2004.

Vivian S. Lamb
Vivian S. Lamb

Subscribed and sworn to before me this 3rd day of May, 2004.

Paula J. Cagle
Notary Public



Commission Expires: My Commission Expires NOV. 25, 2006

My Commission Expires NOV. 25, 2006



PHIL BREDESEN
GOVERNOR

STATE OF TENNESSEE
DEPARTMENT OF FINANCIAL INSTITUTIONS
SUITE 400, NASHVILLE CITY CENTER
511 UNION STREET
NASHVILLE, TENNESSEE 37219
(615) 741-2236 FAX (615) 741-2883

KEVIN P. LAVENDER
COMMISSIONER

April 5, 2004

**Board of Directors
Sentinel Trust Company
29 W. Main Street
Hohenwald, TN 38462**

Dear Members of the Board:

It is my understanding that Sentinel Trust Company (STC) serves as the indenture trustee for various high-yield, unregistered municipal and corporate bonds. In some instances, the debtor fails to make the scheduled principal and interest payments and default is declared per the terms of the indenture. Oftentimes the debtor will seek bankruptcy protection, which triggers an automatic stay and prevents any action from creditors until a plan of reorganization, debt restructuring and/or sale of collateral is approved by the bankruptcy court.

Further, it is my understanding that STC, in its role as indenture trustee for the bondholders, in many instances funds various expenses relative to these defaulted issues, such as insurance, security, legal and other professional fees, in an effort to protect the value of the underlying collateral.

I also understand that usually the governing indenture and/or bondholder indemnification will provide for the reimbursement of these expenses from the proceeds of the sale of the collateral. However, since STC maintains insufficient liquidity to fund these expenses, it appears that STC usually "borrows" from other non-related bond issues to fund these expenses. This is accomplished by writing checks and/or executing wires on a pooled demand deposit account held at SunTrust Bank, Orlando, Florida. You have stated that this is "common industry practice". However, it is unclear whether these "borrowings" are permitted per the indenture of the other non-related issues or if the non-related issues receive any monetary benefit.

ATTACHMENT 1

BANK DIVISION
BANKS, SAVINGS BANKS, TRUST COMPANIES
(615) 741-6013

CREDIT UNION DIVISION
(615) 741-5408

LEGAL DIVISION
(615) 741-0348

COMPLIANCE DIVISION
NON-DEPOSITORY LENDERS
(615) 741-3186

Board of Directors
Sentinel Trust Company
April 5, 2004
Page 2

As of the June 13, 2003 examination initiated by this Department, these borrowings or overdrafts were believed to be (\$2,536,376.56). As of August 31, 2003, October 31, 2003 and December 31, 2003, they were believed to be (\$3,027,601.08), (\$3,349,047.82), and (\$2,816,030.80), respectively. See Exhibit A attached.

Therefore, I am requesting you provide this office, within fifteen (15) days of the date of this letter, a written acknowledgement as to the accuracy of my understanding of your company's practices, as described above. In addition, please provide this office, within thirty (30) days of the date of this letter, a written legal opinion addressing the legal basis of such practice.

Should you have any questions please contact Chief Administrator Tod Trulove at (615) 741-6013.

Sincerely,



Kevin P. Lavender

Attachment

KPL/TKT/VL

cc: Danny Bates, President
MTFO
Vivian Lamb

EXHIBIT A

SENTINEL TRUST COMPANY
Defaulted Bond Issues in Overdraft Status

	<u>6/13/2003</u>	<u>8/31/2003</u>	<u>10/31/2003</u>	<u>12/31/2003</u>
423342020 Dade City FL Series 98 Bond Fund	\$ -70,836.61	\$ -82,056.24	\$ -112,991.51	\$ *
427865010 Jose Eber Salons Inc Bond Fund	-106,834.14	-117,329.78	-120,790.43	-125,954.82
434841010 Ft. Pierce FL Lyford Cove Bond FD A	-223,229.84	-257,212.40	-268,251.96	-285,818.94
442791010 Hernando Co FL Bond Fund	-480,862.29	-539,467.46	-603,283.03	-649,884.26
447271001 Jefferson Co AR TAS account	-145,623.11	-233,383.86	-235,514.28	-294,853.60
452343010 Lee Co AL GWC Foods Bond Fund	-394,226.16	-435,060.27	-476,186.29	-511,543.40
453039010 Liberty Co GA Midway Bond Fd	-27,240.52	-33,813.22	-29,113.32	-32,774.15
465259010 Newton Co IN Americare Bond Fund	-35,087.02	-68,834.94	Account was closed.	
478219020 Rusk County Texas Choice Comm Bond Fd	-133,125.35	-151,415.93	-177,954.80	-202,719.66
487590010 Tarrant Co TX Comm Hlth Ser91 Bond	-252,679.08	-280,563.14	-331,218.57	-408,881.40
493,800010 Washington Co MS M-F Hsg GRCC	<u>-666,632.44</u>	<u>-828,463.84</u>	<u>-993,749.63</u>	<u>-303,600.57</u>
TOTAL	\$-2,536,376.56	\$-3,027,601.08	\$-3,349,047.82	\$-2,816,030.80

*This account reflected a positive balance of 87,830.06 as of the 12-31-2003 Trust Department Balance Sheet Detail.